Report

of the

Examination of

Waukesha County Mutual Insurance Company

Waukesha, Wisconsin

As of December 31, 2000

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State of Wisconsin / OFFICE OF THE COMMISSIONER OF INSURANCE

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September 28, 2001

Honorable Connie L. O'Connell
Commissioner of Insurance
State of Wisconsin
121 East Wilson Street
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Commissioner:

In accordance with your instructions, an examination has been performed as of December 31, 2000, of the affairs and financial condition of

WAUKESHA COUNTY MUTUAL INSURANCE COMPANY
Waukesha, Wisconsin

and the following report thereon is respectfully submitted:

I. INTRODUCTION

The last examination of this company was made in 1996 as of December 31, 1995. The current examination covered the intervening time period ending December 31, 2000, and included a review of such subsequent transactions deemed essential to complete this examination.

The Summary of Examination Results contains elaboration on all areas of the company's operations. Special attention was given to the action taken by the company to satisfy the recommendations and comments made in the previous examination report.

The company was originally organized as a town mutual insurance company on February 28, 1874 under the provisions of the then existing Wisconsin Statutes. The original name of the company was the Farmers Mutual Fire Insurance Company of the Town of Waukesha. Subsequent amendments to the company's articles and bylaws changed the company's name to that presently used.

During the period under examination, there was one amendment to the articles of incorporation and one amendment to the bylaws. The articles of incorporation were amended to make it easier to change the number of directors by authorizing a Board of Directors whose members, qualifications and terms shall be established in accordance with the corporation's bylaws. Related bylaws were amended by establishing that the number of directors after 1999 shall be fixed by resolution adopted by a majority of the board in office, but shall not be less than seven nor more than twelve.

A review of the certificate of authority revealed that the company is currently licensed to write business in the following counties:

Jefferson, Milwaukee, Ozaukee, Racine, Sheboygan,
Walworth, Washington, and Waukesha

The company is currently licensed to write property, including windstorm and hail, and nonproperty insurance.

A review was made of the policy and application forms currently used by the company. The company issues an approved policy with or without endorsements for terms of one year with premiums payable on the advance premium basis. Policy fees charged policyholders are retained by the company.

Business of the company is acquired through 10 agencies representing 28 agents, 2 of whom are directors of the company. Agents are presently compensated for their services as follows:

Type of Policy	**Compensation**
All new and renewal business	15%

Agents do not have authority to adjust losses. The company employs an independent adjuster for evaluation and adjustment of all property loss claims. Adjusters receive $45-50 / hour for each loss adjusted plus 15-22% for office expense, depending on whether the claim is less than or greater than $5,000. All non-property losses are adjusted by the reinsurer.

Policyholders may participate in the management and control of the company by attending and voting at all annual or special meetings of the members. No member may vote by proxy. The annual meeting of the company for the election of directors and special meetings of the company are held in accordance with its articles of incorporation.

Board of Directors

The board of directors consists of 11 members divided into three classes. One class is elected at each annual meeting for a term of three years. Vacancies on the board may be filled by the directors for the interim to the next annual meeting when a director shall be chosen for the unexpired term.

The current board of directors consists of the following policyholders of the company:

Name	Principal Occupation	Residence	Expiry
Alvin Basse	Farmer	Muskego	2002
William Bloede	Retired Banker	Waukesha	2001
Janice Buth	Bookkeeper	Pewaukee	2003
Randall Craig	Farmer	Big Bend	2001
David Guthrie	Farmer	Big Bend	2002
Curtis Manke*	Insurance Agent/ Company Secretary/Treasurer	Waukesha	2003
William Orchard	Farmer	Eagle	2001
Willard Parry*	Retired	Hartland	2003
Henry Rosenow Jr.	Farmer	Oconomoc	2002
David Swan	Farmer	Pewaukee	2003
Melvin Trapp	Construction Expeditor	Hartland	2001

Directors who are also agents are identified with an asterisk.

Members of the board currently receive $50 for each meeting attended and $.325 per mile for travel expenses.

Officers

Officers are elected by the board of directors from among its members and hold office for one year or until their successors are duly elected and qualified.

Officers serving at the present time are as follows:

Name	Office	Annual Salary
William Parry	President	$ 1,250
Henry Rosenow Jr.	Vice President	0
Curtis Manke	Secretary / Treasurer	25,000

The Secretary / Treasurer is the legal tenant of the office space that is occupied by the company. The rental of these premises for the operations of his personal insurance agency business pre-dates his employment with the company. Waukesha County Mutual Insurance pays the rent on the property under a lease agreement with the Secretary/Treasurer as his sub-tenant, effective March 2001. The company's compensation to the Secretary/Treasurer includes his use of this company office space, as well as, the funding of the company's SEP pension plan benefit in addition to the salary listed above.

Committees of the Board

The company's bylaws allow for the formation of certain committees by the board of directors. The committees at the time of the examination are listed below:

Adjusting Committee	Investment Committee	Budget/Long Range Plan Committee
Janice Buth	William Bloede	Randall Craig
Randall Craig	Curtis Manke	William Bloede
David Guthrie		Melvin Trapp

Growth of Company

The growth of the company during the past five years as compiled from its filed annual statements was as follows:

Year	Net Premiums Earned	Net Losses and LAE Incurred	Policies In Force	Net Income	Admitted Assets	Policyholders' Surplus
1996	$166,605	$68,597	711	$54,970	$1,326,023	$1,162,751
1997	148,711	95,313	695	24,988	1,347,543	1,182,160
1998	162,840	157,743	658	(29,024)	1,366,987	1,182,526
1999	164,744	139,531	654	(33,226)	1,285,258	1,145,194
2000	177,551	68,069	640	41,343	1,347,369	1,210,580

The ratios of premiums written, gross and net, to surplus as regards policyholders during the past five years were as follows:

Year	Gross Premiums Written	Net Premiums Written	Ending Surplus	Writings Ratios Gross	Writings Ratios Net
1996	$321,045	$186,604	$1,162,751	28%	16%
1997	287,571	145,020	1,182,160	24	12
1998	281,636	165,490	1,182,526	24	14
1999	276,880	148,312	1,145,194	24	13
2000	267,621	165,390	1,210,580	22	14

For the same period, the company's operating ratios were as follows:

Year	Net Losses and LAE Incurred	Other Underwriting Expenses Incurred	Net Earned Premiums	Loss Ratio	Expense Ratio	Composite Ratio
1996	$68,597	$115,142	$166,605	41%	62%	103%
1997	95,313	107,528	148,711	64	74	138
1998	157,743	110,556	162,840	97	67	164
1999	139,531	122,521	164,744	85	83	167
2000	68,069	133,441	177,551	38	81	119

The company has continued to experience high expense ratios in recent years. Analysis of company financial trends indicated that its Underwriting Expense Ratio increased from 62% to 81% during the period under examination. The town mutual industry average expense ratio has been in the 40-50% range during this period. Approximately 60% of the expenses relate to commissions, salary and rent.

The company's costs reflect the impact of fixed expenses on decreasing premium written and policies in-force, which, in turn, is affected by the competition associated with the company's location in the greater Milwaukee area.

II. REINSURANCE

The examiners' review of the company's reinsurance portfolio revealed there is currently one ceding treaty. The treaty contained a proper insolvency clause and complied with s. Ins 13.09 (3), Wis. Adm. Code, concerning maximum wind loss. Company retentions of risk complied with s. Ins 13.06, Wis. Adm. Code.

Reinsurer:	Wisconsin Reinsurance Corporation
Effective date:	January 1, 2000
Termination provisions:	Any January 1st subject to 90 days prior written notice by either party

The coverages provided under this treaty are summarized as follows:

1.	Type of contract:	Excess of Loss Reinsurance
	Lines reinsured:	All nonproperty business
	Company's retention:	$750 in respect to each and every loss occurrence, including loss adjustment expenses
	Coverage:	100% of each and every loss occurring on the business including loss adjustment expenses in excess of the company's net retention, subject to the maximum limits of: a. $1,000,000 per occurrence, single limit, combined for bodily injury and property damage liability b. $1,000,000 split limits, in any combination of bodily injury and property damage liability c. $5,000 medical per person; $25,000 per accident
	Reinsurance premium:	75% of premium written for each and every policy issued
2.	Type of contract:	Class B First Surplus
	Lines reinsured:	All property business
	Company's retention:	When the net retention on a policy is $150,000 or more, the company may cede on a pro rata basis up to $800,000. When the net retention is $150,000 or less in respect to a risk, the company may cede up to 50% of such risk. The Annual Aggregate Deductible hereunder is equal to 10% of paid losses and paid loss adjustment expense.
	Coverage:	The Reinsurer shall be liable for the pro rata portion of each and every loss including loss adjustment expense, corresponding to the amount of risk ceded up to $800,000.
	Reinsurance premium:	Pro rata portion of all premiums, fees and assessments corresponding to the amount of each risk ceded
	Ceding commission:	Provisional commission of 15% if the loss ratio is 65% or greater subject to an increase of 1% for each 1% decrease in the loss ratio up to a maximum commission of 35% when the loss ratio is 45% or less.

3.	Type of contract:	Class C Excess of Loss Reinsurance
	Lines reinsured:	All property business
	Company's retention:	$20,000 in respect to each and every risk resulting from one loss occurrence. In addition, the company retains as an Annual Aggregate Deductible an amount equal to $20,000 of loss that would otherwise be recoverable for the annual contract period
	Coverage:	100% of any loss, excluding loss adjustment expense, in excess of $20,000 in respect to each and every risk resulting from one loss occurrence, subject to a reinsurer's limit of liability of $40,000
	Reinsurance premium:	Net premiums written multiplied by the sum of four years' losses incurred divided by the total net premiums for the same period multiplied by a factor of 100/80ths. Minimum Rate: 5.50% of the current net written premiums Maximum Rate: 21.75% of the current net written premium Current annual period rate is 6.00%
4.	Type of contract:	Class C Second Excess of Loss Reinsurance
	Lines reinsured:	All property business
	Company's retention:	$60,000 in respect to each and every risk resulting from one loss occurrence
	Coverage:	100% of any loss, excluding loss adjustment expense, in excess of $60,000 in respect to each and every risk resulting from one loss occurrence, subject to a reinsurers's limit of liability of $90,000
	Reinsurance premium:	3.25% of net premiums written subject to a minimum deposit premium of $5,700
5.	Type of contract:	Class D/E Stop Loss Reinsurance
	Lines reinsured:	All business written by the company
	Company's retention:	Annual aggregate net losses up to 75% of the company's net premium written, subject to a minimum net retention of $130,320
	Coverage:	100% of annual aggregate net losses in excess of retention
	Reinsurance premium:	The net premiums written multiplied by the sum of eight years' losses incurred divided by the total of the net premiums written for the same period, multiplied by a factor of 100/80ths Minimum Rate: 5% of the current net premiums written Maximum Rate: 25% of the current net premiums written Current annual period rate is 5%

III. FINANCIAL DATA

The following financial statements were filed with the Commissioner of Insurance in the company's annual statement at December 31, 2000. Adjustments made as a result of the examination are noted at the end of this section of this report in the area captioned "Reconciliation of Policyholders' Surplus."

Waukesha County Mutual Insurance Company
Statement of Assets and Liabilities
As of December 31, 2000

Assets	**Ledger**	**Nonledger**	**Not Admitted**	**Net Admitted**
Cash Deposited in Checking Account	$ 6,948	$	$	$ 6,948
Cash Deposited at Interest	146,220			146,220
Bonds (at Amortized Cost)	742,836			742,836
Stocks or Mutual Fund Investments (at Market)	404,576			404,576
Premiums and Agents' Balances In Course of Collection	2,357			2,357
Premiums and Agents' Balances & Installments Booked But Deferred Not Yet Due	21,760			21,760
Investment Income Due/Accrued		19,530		19,530
Electronic Data Processing Equipment (Cost Less Accumulated Depreciation)	714			714
Furniture and Fixtures	998		998	
Fire Dues Recoverable	104			104
Reinsurance Premium Recoverable	2,024			2,024
Accounts Receivable - Misc	300			300
TOTALS	$1,328,837	$19,530	$998	$1,347,369

Liabilities and Surplus	
Net Unpaid Losses	$ 16,316
Unpaid Loss Adjustment Expenses	700
Commissions Payable	2,763
Net Unearned Premiums	109,559
Premiums Received in Advance	7,333
Amounts Withheld for the Account of Others	118
TOTAL LIABILITIES	136,789
Policyholders' Surplus	1,210,580
TOTAL	$1,347,369

Waukesha County Mutual Insurance Company
Statement of Operations
For the Year 2000

Net Premiums and Assessments Earned	$177,552
Deduct:	
Net Losses Incurred	46,552
Net Loss Adjustment Expenses Incurred	21,517
Other Underwriting Expenses Incurred	133,441
Total Losses and Expenses Incurred	201,510
Net Underwriting Gain (Loss)	(23,958)
Net Investment Income:	
Net Investment Income Earned	64,281
Net Realized Capital Gains	(18)
Total Investment Income	64,263
Other Income:	
Miscellaneous Income	1,038
Net Investment and Other Income	65,301
Net Income (Loss) Before Policyholder Dividends and Before Federal Income Taxes	41,343
Net Income (Loss) Before Federal Income Taxes	41,343
Federal Income Taxes Incurred	0
Net Income (Loss)	$ 41,343

Waukesha County Mutual Insurance Company
Reconciliation and Analysis of Surplus as Regards Policyholders
For the Five-Year Period Ending December 31, 2000

The following schedule is a reconciliation of surplus as regards policyholders during the period under examination as reported by the company in its filed annual statements.

Surplus as regards policyholders, December 31, 1995		$1,091,421
1996		
Net income (loss)	$54,970	
Net unrealized capital gains or losses	15,882	
Change in nonadmitted assets	478	
Change in surplus as regards policyholders for the year		71,330
Surplus as regards policyholders, December 31, 1996		$1,162,751
1997		
Net income (loss)	$24,988	
Net unrealized capital gains or losses	(5,579)	
Change in nonadmitted assets	0	
Change in surplus as regards policyholders for the year		19,409
Surplus as regards policyholders, December 31, 1997		$1,182,160
1998		
Net income (loss)	$(29,024)	
Net unrealized capital gains or losses	29,390	
Change in nonadmitted assets	0	
Change in surplus as regards policyholders for the year		366
Surplus as regards policyholders, December 31, 1998		$1,182,526
1999		
Net income (loss)	$(33,226)	
Net unrealized capital gains or losses	(4,106)	
Change in nonadmitted assets	0	
Change in surplus as regards policyholders for the year		(37,332)
Surplus as regards policyholders, December 31, 1999		$1,145,194
2000		
Net income	$41,343	
Net unrealized capital gains or losses	25,041	
Change in nonadmitted assets	(998)	
Change in surplus as regards policyholders for the year		65,386
Surplus as regards policyholders, December 31, 2000		$1,210,580

Reconciliation of Policyholders' Surplus

There were no reclassifications or adjustments to surplus as a result of the current examination.

IV. SUMMARY OF EXAMINATION RESULTS

Compliance with Prior Examination Report Recommendations

Comments and recommendations contained in the last examination report and the action taken on them by the company are as follows:

1. Management and Control—It is recommended that the company evaluate its long-term marketing plans, expectations for growth in premiums and policies, any merger possibilities, and long-term personnel needs. After the evaluation, if it appears likely that policy and premium activity will remain near current levels, then the company should take appropriate action to reduce its underwriting expenses.

   Action—Partial Compliance, see Current Examination Results section for further comment.

2. Management and Control—It is recommended that the company negotiate a written agreement for its home office space.

   Action—Compliance was not in place as of 12/31/00, but was subsequently implemented.

3. Underwriting—Since the company does not have a formal inspection procedure for new and renewal business, consideration should be given to the establishment of such a procedure, whereby a sampling of new applications and of renewal business is inspected by committee members independent of the risk under consideration and review.

   Action—Noncompliance, see Current Examination Results section for additional comment.

4. Invested Assets—It is recommended that the company's custodial agreements expressly provide for the fiduciary obligations of the custodian, so that the custodian is obligated to indemnify the company for any loss of securities of the company held in the custodian's custody. It is further recommended that the custodial agreements provide that in the event of a loss of securities for which the custodian is obligated to indemnify the company, the securities shall be promptly replaced or the value of the securities and the value of any loss of rights or privileges resulting from said loss of securities shall be promptly replaced.

   Action—Compliance

5. Cash and Invested Cash—It is recommended that the company perform bank deposit of cash receipts at least weekly, in compliance with s. Ins 13.05 (4) (a). Wis. Adm. Code.

   Action—Compliance

6. Bonds—It is recommended that the company's future investments conform to all town mutual standards and limitations, as provided by s. Ins 6.20, Wis. Adm. Code.

   Action—Compliance

7. Unpaid Loss Adjusting Expense—It is recommended that the company annually report its estimated liability for unpaid loss adjusting expense necessary to settle any losses incurred on or prior to the financial report date in accordance with annual statement instructions.

   Action—Compliance

8. Unearned Premium—It is again recommended that the company request approval by the Commissioner for the company's method of calculating its unearned premium reserve, in compliance with s. Ins 13.08 (4), Wis. Adm. Code.

   Action—Compliance

Current Examination Results

Corporate Records

The minutes of the annual meetings of policyholders and meetings of the board of directors and any committees thereof, were reviewed for the period under examination and also for the subsequent current period.

Biographical data relating to company officers and directors have been reported in accordance with the provisions of s. Ins 6.52, Wis. Adm. Code.

The company has executed formal written agreements with its agents. The contracts include language indicating the agent will represent the company's interests "in good faith."

Management and Control - Business Plan

As previously noted in the report, the five-year period since the prior examination indicates less favorable trends, including a decrease in In-Force policies from 739 to 640, a decrease in Gross Premiums Written from $304,000 to $267,000 and an increase in the Underwriting Expense Ratio from 62% to 81%.

The Board of Directors has established a Vision and Mission Statement as of the August 2000 Directors' Meeting. The Mission Statement's emphasis includes:

- "Innovation in developing and adopting new methods, products and services"
- "Financial stability that will provide for reasonable future growth"

The Board of Directors also adopted a five-year budget. This budget projects a nominal increase in annual gross premiums written, annual operating expense increases of approximately 2% and investment income reductions from prior years, resulting in annual decreases to surplus. Accordingly, it would continue to seem prudent and is recommended that the Board evaluate its longer term plans by building on its recent Misssion Statement objectives and establishing more definitve Business Plans and financial targets to measure performance, including:

- Marketing Plans to achieve premium growth
- Operating Expense reductions to establish a more reasonable expense ratio
- Merger opportunities to spread fixed costs over a larger premium base
- Management succession plans as current management approaches potential retirement

Conflict of Interest

In accordance with a directive of the Commissioner of Insurance, each company is required to establish a procedure for the disclosure to its board of directors of any material interest or affiliation on the part of its officers, directors, or key employees which conflicts or is likely to conflict with the official duties of such person. A part of this procedure is the annual completion of a conflict of interest questionnaire by the appropriate persons. The company has adopted such a procedure for disclosing potential conflicts of interest.

Conflict of interest questionnaires were reviewed for the period under examination. Questionnaire responses do continue to identify the potential conflict of interest due to the Secretary/Treasurer's dual role as Officer of Waukesha County Mutual Insurance and President of the independent Manke Insurance Agency, which serves as an agent for the town mutual. Accordingly, it is recommended that the Board of Director Meeting minutes should reflect the fact that the Secretary/Treasurer abstained from voting on potential conflict of issues relating to approval of Town Mutual Officer compensation and Office Space Lease expense, as required under s. 611.60 (2) Wis Stat.

Fidelity Bond and Other Insurance

The company is afforded coverage under the terms of the following bonds or contracts and has complied with s. Ins 13.05 (6), Wis. Adm. Code, which sets forth the minimum requirements for fidelity bond coverage:

Type of Coverage	Coverage Limits
Fidelity Bond	$250,000
Business Owners' Policy:	
▪ Business Personal Property	10,000
▪ Money and Securities On-Premise	10,000
▪ Money and Securities Off-Premise	5,000
▪ Fire Damage	100,000
▪ Minicomputer Coverage	10,000
Professional Liability and Director's And Officers Liability	1,000,000 each claim 1,000,000 policy aggregate per policy period
Worker's Compensation and Employers Liability:	
▪ Bodily Injury by Accident	100,000 each accident
▪ Bodily Injury by Disease	100,000 each employee 500,000 policy limit

Underwriting

The company utilizes WRC guidelines for its liability insurance business and has a written general underwriting guideline statement for its property business. The company indicated that it has not complied with prior exam recommendations to implement formal inspection procedures for new and renewal business and does not feel that such procedures are warranted. Current underwriting guidelines do require pictures on all new business. New or renewal business is selectively inspected when a major change is made to existing policies or in cases where management is not familiar with the insured risk or has questions which warrant review. Claims are reviewed by an external adjuster with Adjusting Committee oversight. The above company underwriting procedures do not seem unreasonable, given the company's decreasing Premium Written and In-Force volume, generally positive Net Loss & LAE Ratio trends and external claim adjuster review procedures. Accordingly, compliance with this prior recommendation is waived.

Claims Adjusting

The company has an adjusting committee consisting of at least three directors as required by s. 612.13 (4), Wis. Stat. The function of this committee is to adjust or supervise the adjustment of losses.

Accounts and Records

The examiners' review of the company's records indicated that the company is in compliance with s. Ins 13.05, Wis. Adm. Code, which sets forth the minimum standards for the handling of cash and recording of cash transactions by town mutual insurance companies. The examiners noted the following:

1. A proper policy register is maintained
2. A proper cash receipts journal is maintained
3. A proper cash disbursements journal is maintained
4. A proper general journal is maintained
5. A proper general ledger is maintained

The current exam included a review of income and disbursement items. Cash receipts were traced from source records and the proper recording and eventual deposit thereof ascertained. Negotiated checks issued during the period under examination were reviewed, test checked for proper endorsement, and traced to cash records. The verification of assets and determination of liabilities were made as of December 31, 2000.

The company is audited annually by an outside public accounting firm.

EDP Environment

Company personnel were interviewed with respect to the company's Electronic Data Processing environment. WRC systems are used for both Policyholder and General Ledger information. Limited staffing requires access to the computer by both the Office Administrator and Secretary / Treasurer. Virus protection systems were apparently never restored after system problems some time ago.

Disaster Recovery Plan

A disaster recovery plan identifies steps to be performed in case the company loses a key employee, is not able to access its computer, information on its computer was lost, or the office building was destroyed, to name a few contingencies. The company follows informal disaster recovery practices which include:

- On-site backup of daily activity on "Day of Week" disks with a second copy stored off-premise at the Office Administrator's home
- On-site backup of monthly reports activity on a "Quarterly Activity" set of disks with no off-premise backup
- No systems software backup with expected reliance on the vendor

The company has not formally documented its disaster recovery procedures and practices. Accordingly, it is recommended that disaster recovery procedures should be formalized into some form of checklist documentation to:

- Identify adequate on-site and off-site premise backup requirements for both daily and monthly processing of company records
- Define and confirm system backup reliance and relationships with the vendor
- Provide for periodic test checking to ensure adequacy
- Ensure understanding and provide for documented reference in the event that regular staff are not available

It is also recommended that Virus Protection software be reinstalled along with provisions for periodic maintenance and update.

Invested Assets

Section 610.23, Wis. Stat., requires insurers to hold all investments and deposits of its funds in its own name except that:

> (1) Securities kept under a custodial agreement or trust arrangement with a bank or banking and trust company may be issued in the name of a nominee of the bank or banking and trust company; and
>
> (2) Any insurer may acquire and hold securities in bearer form.

For securities not held under a custodial agreement or trust arrangement with a bank or banking and trust company, s. Ins 13.05 (4), Wis. Adm. Code, requires that:

> Non-negotiable evidences of company investments such as registered bonds, certificates of deposits, notes, etc., shall be maintained in a safe or vault with adequate safety controls or in a safety deposit box in a bank. Negotiable evidences of company investments shall be maintained in a safety deposit box in a bank. Access to a company safety deposit box containing negotiable securities shall require the presence and signature of at least 2 officers, directors or employees of the company.

The company is in compliance with these requirements.

The company's invested assets are maintained in the custody of a bank under a custodial agreement. Examination review indicated that this custodial agreement was updated since the prior exam to better address the custodian's fiduciary responsibilities.

Examiner review indicated that the Company's Investment Policy Statement as referenced in the Annual Statement Interrogatories refers to Marine Trust Company Investment Manager Services executed in 1987. The company's current Liquidity Management Agreement executed in 1993 authorizes Banc One Investment Advisors Corporation to act as the company's investment agent, based on reference to a related Liquidity Management Account Investment Guideline Statement. Company management was unable to produce a copy of the above Liquidity Management Account Investment Guideline Statement or a signed copy of the overall Liquidity Management Agreement. Accordingly, Investment Policy review and update was recommended. Subsequent to the completion of the exam fieldwork, the Company complied with these recommendations, including:

- Update of the Investment Policy Statement with Marine Trust, which is the predecessor of Banc One, to support current Banc One relationships
- Follow-up to obtain and review a signed copy of the Banc One Liquidity Management Agreement and supporting Account Investment Guidelines

Future Annual Statement Interrogatory completion to reflect current investment policy is expected.

Transition into the New Investment Rule

On January 1, 1996, the investment rule for town mutuals was amended to allow town mutuals to invest in common stocks, common stock mutual funds, and other higher risk investments (referred to as "Type 2") provided that the town mutual has a sufficient amount of lower risk investments (referred to as "Type 1"). A town mutual may invest in Type 2 securities only if it already has sufficient Type 1 investments. Type 1 investments must equal or exceed the greater of items 1, 2, or 3.

1.	Liabilities plus $300,000	$436,789
2.	Liabilities plus 33% of gross premiums written	225,104
3.	Liabilities plus 50% of net premiums written	219,484
4.	Amount required (greater of 1, 2, or 3)	436,789
5.	Amount of Type 1 investments as of 12/31/2000	919,379
6.	Excess or (deficiency)	$482,590

The company has sufficient Type 1 investments.

The new investment rule prescribes that a town mutual shall divest any investment which does not comply with the rule within three years of its noncompliance, unless the Commissioner permits a longer period or requires a shorter period. Currently the company has one mutual fund investment, with a statement value of $85,620, which had a Morningstar 3-star rating in 2000 and as of the current exam. It also has a mutual fund investment, with a statement value of $14,799, which had a Morningstar 3-star rating in 1999-2000, but was upgraded to a four-star rating as of the exam. The company has chosen to use the three-year divestiture rule. Accordingly, continued monitoring of these investments for compliance with mutual fund rating requirements is suggested, since they have been in/out of compliance during the last several years.

ASSETS

Cash and Invested Cash **$153,168**

The above asset is comprised of the following types of cash items:

Cash deposited in banks-checking accounts	$ 6,948
Cash deposited in banks at interest	146,220
Total	$153,168

Cash deposited in banks subject to the company's check and withdrawal consists of one bank account. Verification of this checking account balance was made by obtaining confirmation directly from the depository and reconciling the amounts shown thereon to company records.

Cash deposited in banks at interest represents the aggregate of two deposits in two depositories. Deposits were verified by tracing the respective Certificates of Deposit to inclusion on the company's investment custodial statement. No interest was received during the year 2000. Rates of interest earned on cash deposits ranged from 7.322% to 7.991%. Accrued interest on cash deposits totaled $6,502 at year-end.

Book Value of Bonds **$742,836**

The above asset consists of the aggregate book value of bonds held by the company as of December 31, 2000. Bonds owned by the company are held under the custody of a bank trust company.

Bonds were not physically inspected by the examiners, but were verified by review of the custodian's year-end statement of the company's investments. Selected bond purchases and sales for the period under examination were also checked to the custodian's account statements. The company's investment in bonds was in conformance with Wisconsin Statutes and the rules of the Commissioner of Insurance as regards investments made by town mutual insurers.

Interest received during 2000 on bonds amounted to $55,960 and was traced to cash receipts records. Accrued interest of $12,478 at December 31, 2000, was checked and allowed as a nonledger asset.

Stocks and Mutual Fund Investments **$404,576**

The above asset consists of the aggregate market value of stocks and mutual funds held by the company as of December 31, 2000. Stocks owned by the company are maintained at a bank under its custodial trust agreement.

Stocks and mutual funds were verified to inclusion on the company's year-end custodial statement. There were no significant stock or mutual fund purchases and sales for 2000. The company's investment in stocks and mutual funds was in conformance with Wisconsin Statutes and the rules of the Commissioner of Insurance as regards investments made by town mutual insurers.

Dividends received during 2000 on stocks and mutual funds amounted to $17,148 and were traced to custodial cash receipts records. Accrued dividends of $550 at December 31, 2000, were checked and allowed as a nonledger asset.

Agents' Balances or Uncollected Premiums **$24,117**

The above ledger asset includes $2,357 of Agents' Balances in Course of Collection representing amounts due from agents or policyholders which are not in excess of 90 days past due at year-end. A review of individual agent's accounts for subsequent receipt of premium payments verified the accuracy of this asset.

The above ledger account also includes $21,760 of premiums billed, but not due until after year-end. These Deferred Premiums were verified by tracing a sample of accounts to policyholder files and statement billings as of 12/31/00 for payments not yet due.

Investment Income Due and Accrued **$19,530**

Interest due and accrued on various assets of the company as of December 31, 2000 consisted of the following:

Cash on Deposit	$ 6,502
Bonds	12,478
Stock / Mutual Funds	550
Total	$19,530

Accrued income amounts were verified by recalculation.

Electronic Data Processing Equipment **$714**

This asset consists of computer equipment, excluding software and net of accumulated depreciation, owned by the company at December 31, 2000. The asset was verified by review of company fixed asset records and has been allowed as an admitted asset in accordance with annual statement requirements.

Equipment, Furniture, and Supplies **$998**

This asset consists of $998 of office equipment owned by the company at December 31, 2000. In accordance with annual statement requirements, this amount has been deducted as an asset not admitted.

Fire Dues Recoverable **$104**

This asset represents the fire department dues recoverable at December 31, 2000. The examiners reviewed the company's fire department dues calculation and found this asset to be correctly calculated and reflective of an overpayment of fire dues.

Reinsurance Premium Recoverable **$2,024**

This asset consists of amounts due to the company at December 31, 2000 relating to reinsurance overpayments which occurred on or prior to that date. The recoverable consisted of the following classes of reinsurance coverage and corresponding balances:

Reinsurance Coverage	Balance Recoverable
Class A Liability	$ 724
Class C Excess of Loss	400
Class C Second Excess of Loss	400
Class D/E Stop Loss	500
Total	$2,024

Review of subsequent cash receipts and reinsurance account reconciliations verified the amount of this asset.

Other Accounts Receivable **$300**

This asset consists of monthly town mutual reimbursements from the Manke Agency for sharing of administrative services. The balance was verified by tracing to subsequent cash receipts.

LIABILITIES AND SURPLUS

Net Unpaid Losses **$16,316**

This liability represents losses incurred on or prior to December 31, 2000, and remaining unpaid as of that date. The examiners' development of unpaid losses is compared with the amount estimated by the company in the following schedule.

	Company Estimate	Examiners' Development	Difference
Incurred But Unpaid Losses	$43,750	$41,259	$2,491
Less:			
Reinsurance Recoverable on Unpaid Losses	27,434	27,173	(261)
Net Unpaid Losses	$16,316	$14,086	$2,230

The examiners developed this liability by totaling actual loss payments made through the development period on those losses incurred on or prior to December 31, 2000. To the actual paid loss figures was added an estimated amount for those 2000 and prior losses remaining unpaid at the examination date. Surplus was not adjusted because the above difference is reflective of a redundancy in reserves which was not considered material for purposes of the examination.

The examiners' review of claim files included open claims, paid claims, claims closed without payment, and all claims which were denied during the examination period. The review indicated that claims are investigated and evaluated properly and that payments are made promptly and in accordance with policy provisions upon the submission of a proper proof of loss. In addition, the review of claims handling procedures and files revealed the following:

1. A proper loss register is maintained.
2. Claim files contained sufficient investigatory data and documentation to verify settlement payments or reserve estimates.
3. Proofs of loss were properly signed.

Unpaid Loss Adjustment Expenses **$700**

This liability represents the company's estimate of amounts necessary to settle losses which were incurred prior to December 31, 2000, but which remained unpaid as of year-end. The methodology used by the company in establishing this liability is based on review of the development of losses and loss adjustment expense on 2000 and prior claims paid by the company.

The examiners' analysis of expenses incurred in the current year related to the settlement of prior year losses, as well as estimates of amounts necessary to settle any prior losses remaining unpaid at the examination date, determined this liability to be adequately stated.

Commissions Payable **$2,763**

This liability represents the company's commissions liability for 2000 commissions due and payable to company agents at December 31, 2000. Supporting commission register records and subsequent cash disbursement records were reviewed to verify the above amount.

Unearned Premiums **$109,559**

This liability represents the reserve established for unearned premiums in compliance with s. Ins 13.08 (3), Wis. Adm. Code. This reserve was established using a daily pro rata methodology, which was previously approved by this office. Unearned premiums were verified based on recalculation and validation of sample in-force premiums to policyholder files.

Premiums Received In Advance **$7,333**

This account represents the liability for premiums received by the company in 2000 for policy effective dates in 2001. These advance premiums were validated by tracing selected premiums to cash receipts records.

Amounts Withheld for the Account of Others **$118**

This liability represents state withholding tax payroll deductions in the possession of the company at December 31, 2000. Review of subsequent cash disbursement records verified this balance.

Other Liabilities - Accounts Payable **$0**

This liability typically represents anticipated expense items payable by the company for services as of December 31, 2000, which will not be billed or paid until the subsequent year. Review of cash disbursements in 2001 indicated incurrence of expenses related to external accounting services for 2000 in the amount of $4700. Although these expenses do not require surplus adjustment based on materiality, it is suggested that year-end accounting provisions should more appropriately recognize an accrual for major expenses such as CPA Audit fees.

V. CONCLUSION

Waukesha County Mutual Insurance Company reported admitted assets of $1,347,369, liabilites of $136,789 and surplus of $1,210,580 as of the current examination. From an overall solvency perspective, the company has continued to realize an increase in surplus during the period since the prior examination of approximately 10%. An underwriting loss has been experienced each year. However, due to investment income, positive net income has been reported in all years except 1998 and 1999.

From an underwriting perspective, the company has experienced a decrease in gross premiums written and policies in-force during this period. Prior examination results have noted higher than normal underwriting expenses attributed, in part, to the impact of fixed costs in relation to decreasing premium volume and the overall competition in the greater Milwaukee geographic market area in which the company operates. In that regard, the underwriting expense ratio has continued to increase from 62% to 81% since the prior examination.

Examination review indicated that the company was in substantial compliance with the prior exam recommendations.

The current examination made three recommendations and two suggestions. The major recommendation relates to the continued observations regarding Management and Control - Business Plans. The Board of Directors did adopt a Mission Statement since the prior exam to partially address prior recommendations in this area. Five-year Operating Budgets project nominal annual increases in premiums written along with operating expense increases and reductions in investment income, which has sustained company net income in the past. These projections indicate that it will continue to be a challenge to spread increasing fixed expenses over a broader base of business.

The current examination recommends that company management and the Board of Directors build on its recent Mission Statement objectives to support and provide for reasonable future growth by establishing more definitive financial performance targets and measurement criteria to achieve and sustain growth, in the best interests of all policyholders.

VI. SUMMARY OF COMMENTS AND RECOMMENDATIONS

1. Page 14 - Management and Control - Business Plan—It is recommended that the Board evaluate its longer term plans by building on its recent Mission Statement objectives and establishing more definitive Business Plans and financial targets to measure performance, including:

   - Marketing Plans to achieve premium growth
   - Operating expense reductions to establish a more reasonable expense ratio
   - Merger opportunities to spread fixed costs over a larger premium base
   - Management succession plans as current management approaches potential retirement

2. Page 15 - Conflict of Interest—It is recommended that the Board of Director minutes reflect the fact that the Secretary/Treasurer abstained from voting on potential conflict of interest issues relating to Town Mutual Officer compensation and Office Space Lease expense, as required under s. 611.60 Wis. Stat.

3. Page 17 - EDP Disaster Recovery Plan—It is recommended that disaster recovery procedures be formalized into some form of checklist documentation to:

   - Identify adequate on-site and off-site premise backup requirements for both daily and monthly processing of company records
   - Define and confirm system backup reliance and relationships with the vendor
   - Provide for periodic test checking to ensure adequacy
   - Ensure understanding and provide for documented reference in the event that regular staff are not available

   It is also recommended that Virus Protection software be reinstalled along with provisions for periodic maintenance and update.

4. Page 19 - Transition into the Investment Rule—It is suggested that the company continue monitoring investments for mutual fund rating requirements, since two of its mutual funds have been in/out of compliance during the last several years.

5. Page 24 - Accounts Payable—It is suggested that year-end accounting provisions should more appropriately recognize an accrual for major expenses, such as CPA Audit fees.

VII. ACKNOWLEDGMENT

The courteous cooperation extended to the examiners by the company's personnel is hereby acknowledged.

In addition to the undersigned, DuWayne A. Kottwitz of the Office of the Commissioner of Insurance, State of Wisconsin, participated in the examination:

Respectfully submitted,

Tom M. Janke
Examiner-in-Charge